

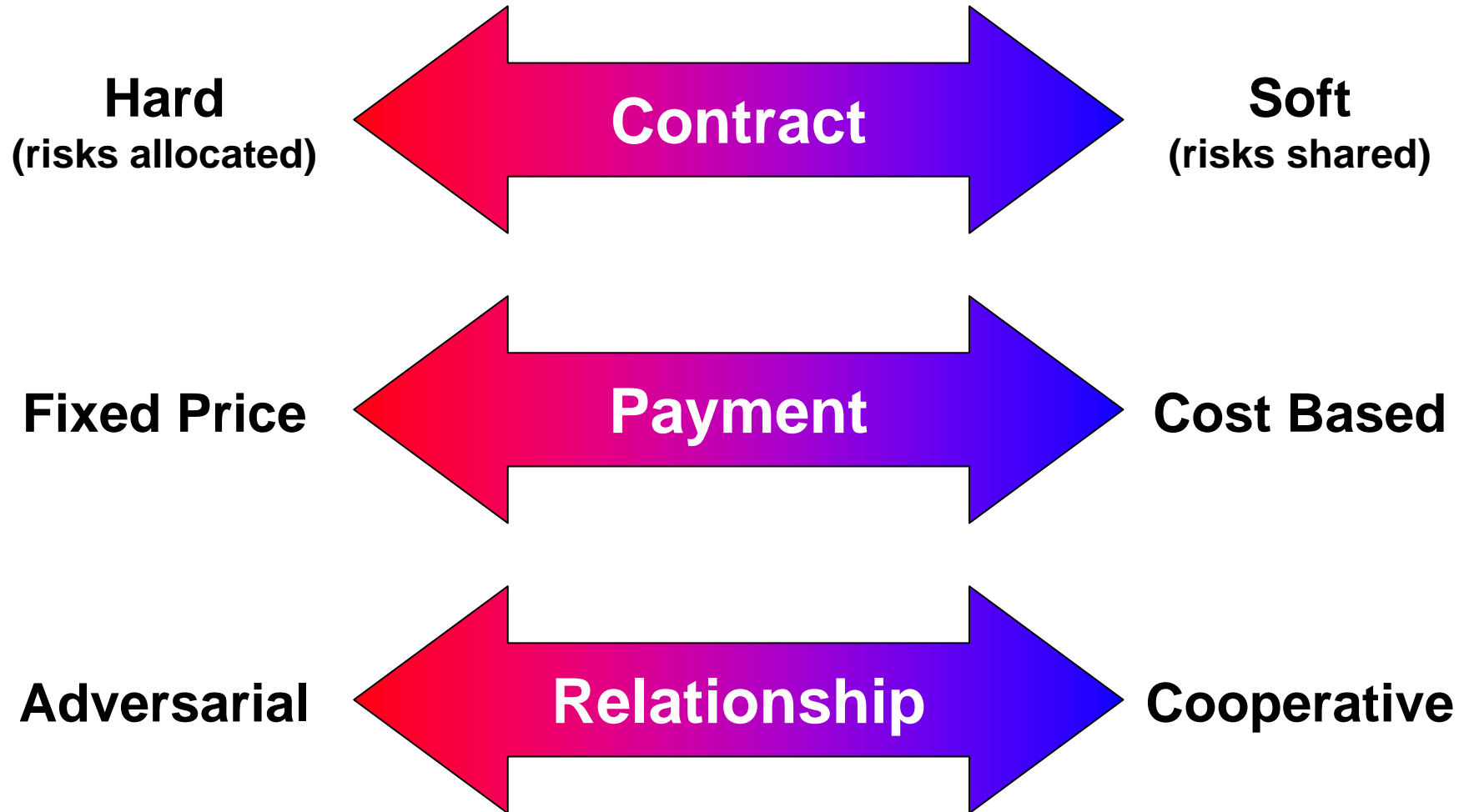
Contract Types and Contract Management

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VGSO Seminar
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Contract Types and Contract Management

- + Contract Types, Relationships and Enhancing Value
- + Contract Types – A new view
 - What does this mean for contract managers?
- + Maintaining and Enhancing Value through Contract Management – Some Issues:
 - Enforcing the contract
 - Single points of contact
 - People/firms changing sides
 - Shopping lists

Contract Types – An Old-fashioned View



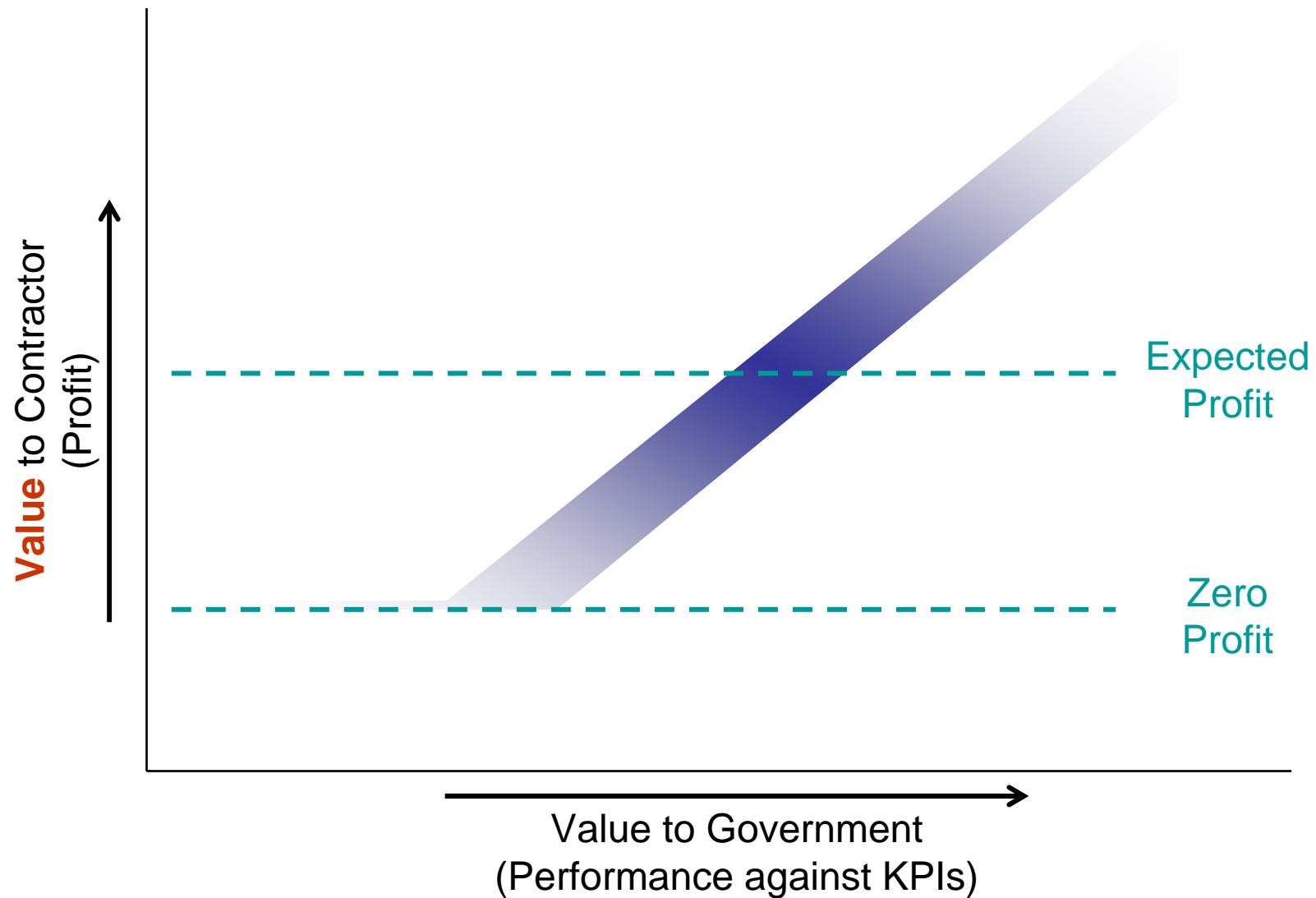
“Hard” Contracts, “Soft” Contracts, PPPs

- + “Hard” contracts include:
 - Construct to design
 - Design and construct
- + “Soft” contracts include:
 - Cost plus
 - Project alliances
- + Which category do public private partnerships fit into?

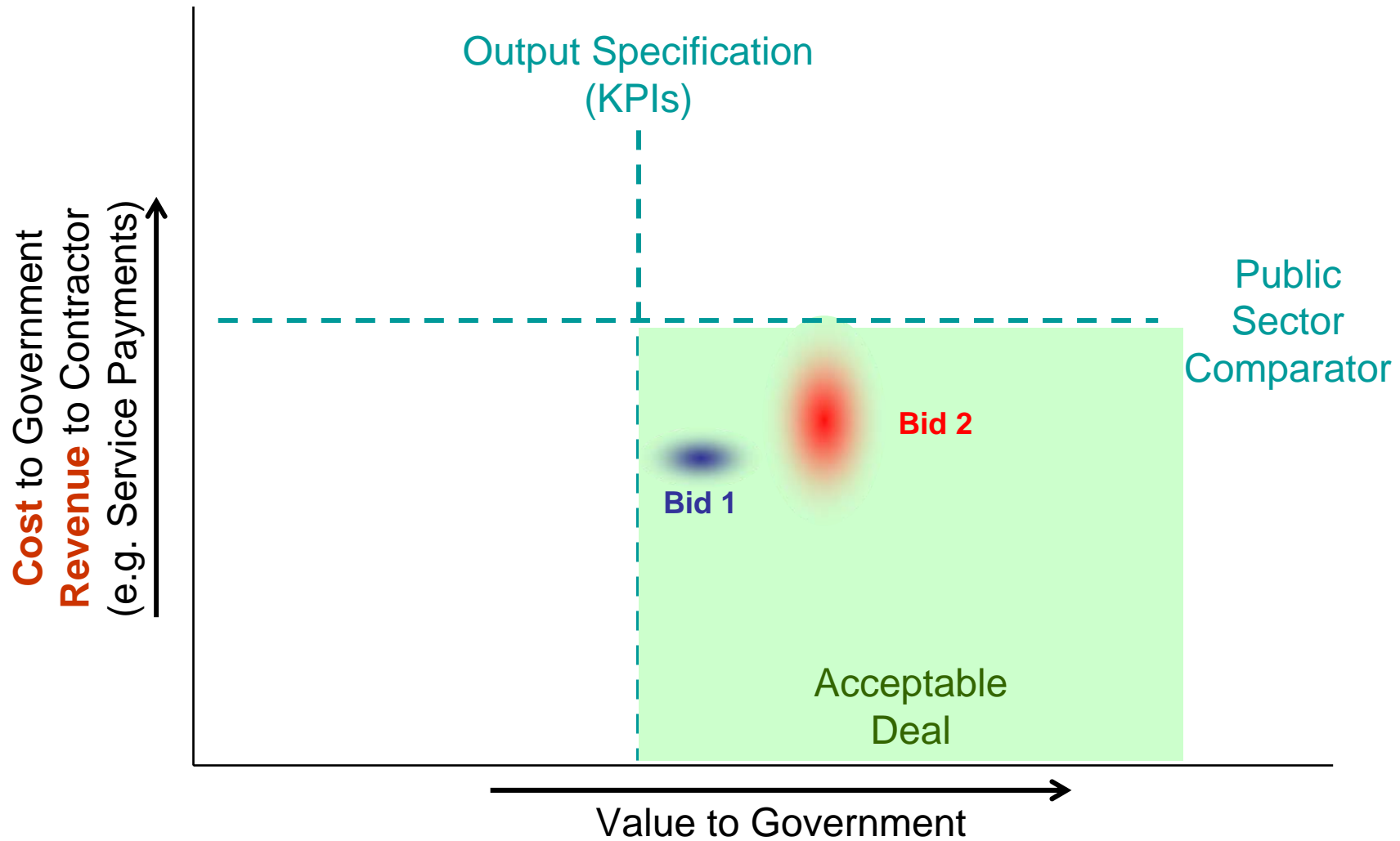
PPP Contracts – “Hard” or “Soft”

- + PPPs are hard money (fixed price) contracts based on risk allocation
- + However:
 - A 25+ year adversarial relationship is unlikely to be satisfactory
 - Experience shows better outcomes can be driven through cooperation
 - Experience shows the nature of the relationship can change from one phase of the contract to another

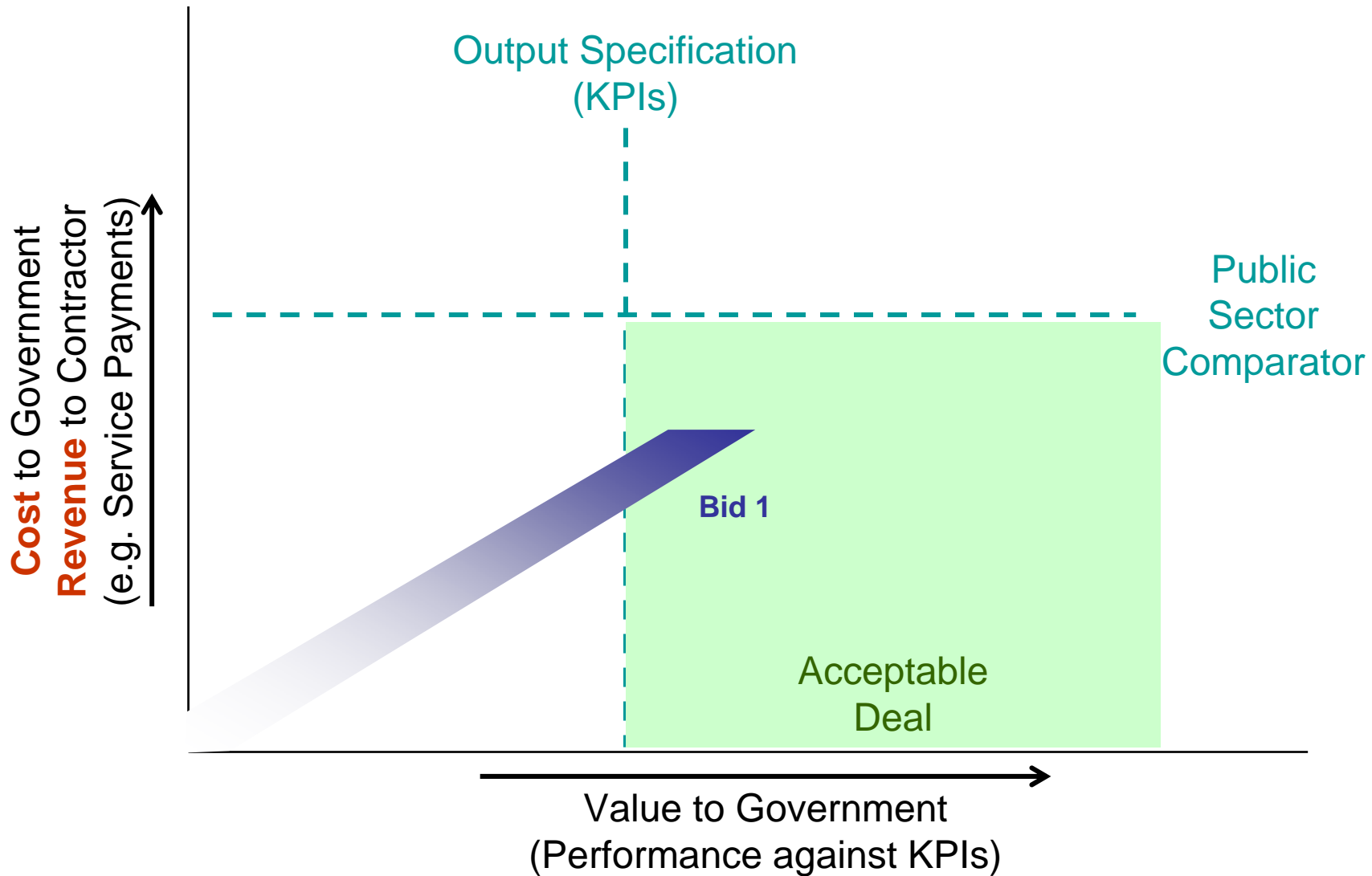
Project Alliance Outcomes



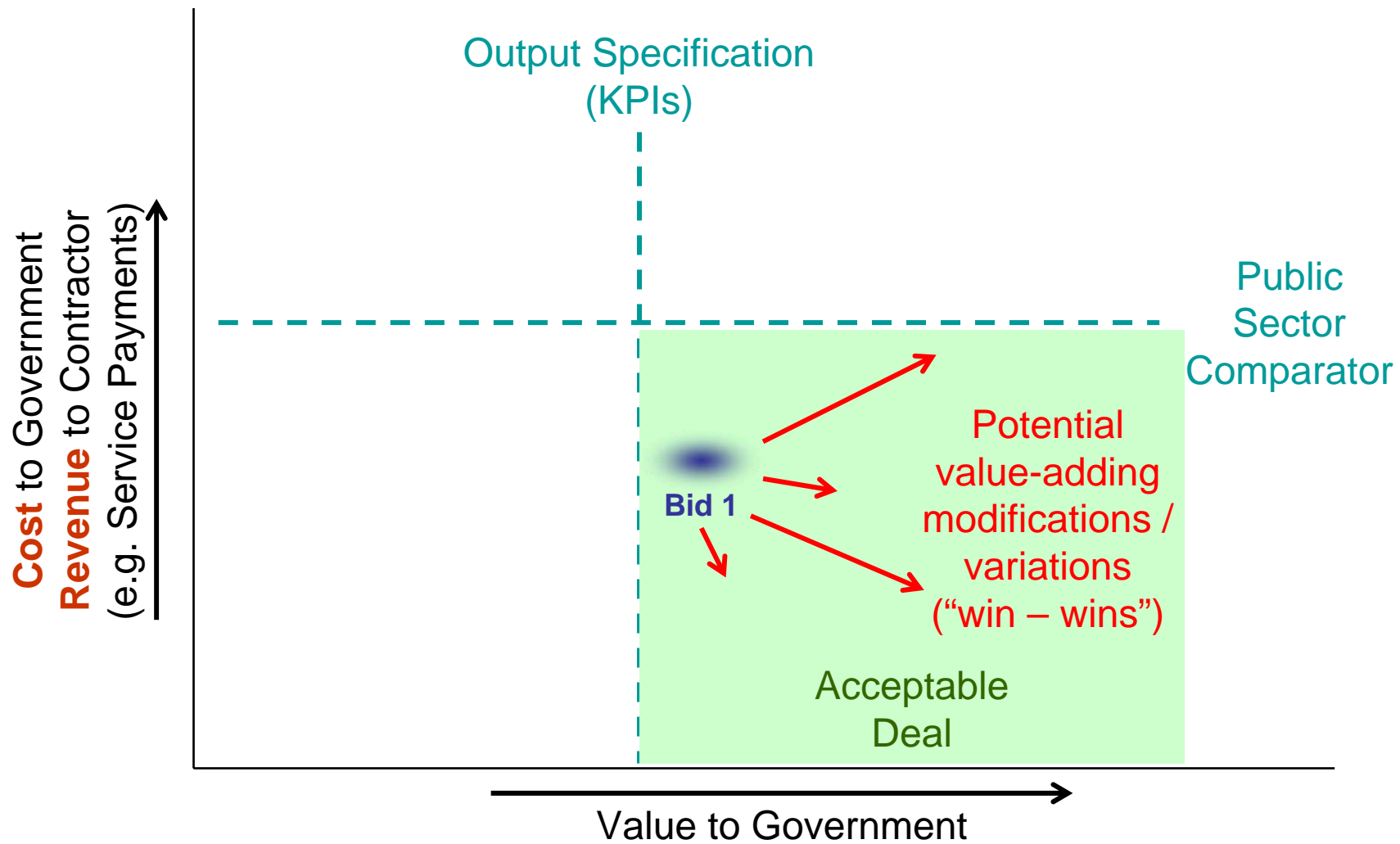
PPPs – Contracted Outcome



PPPs – Payment Mechanism



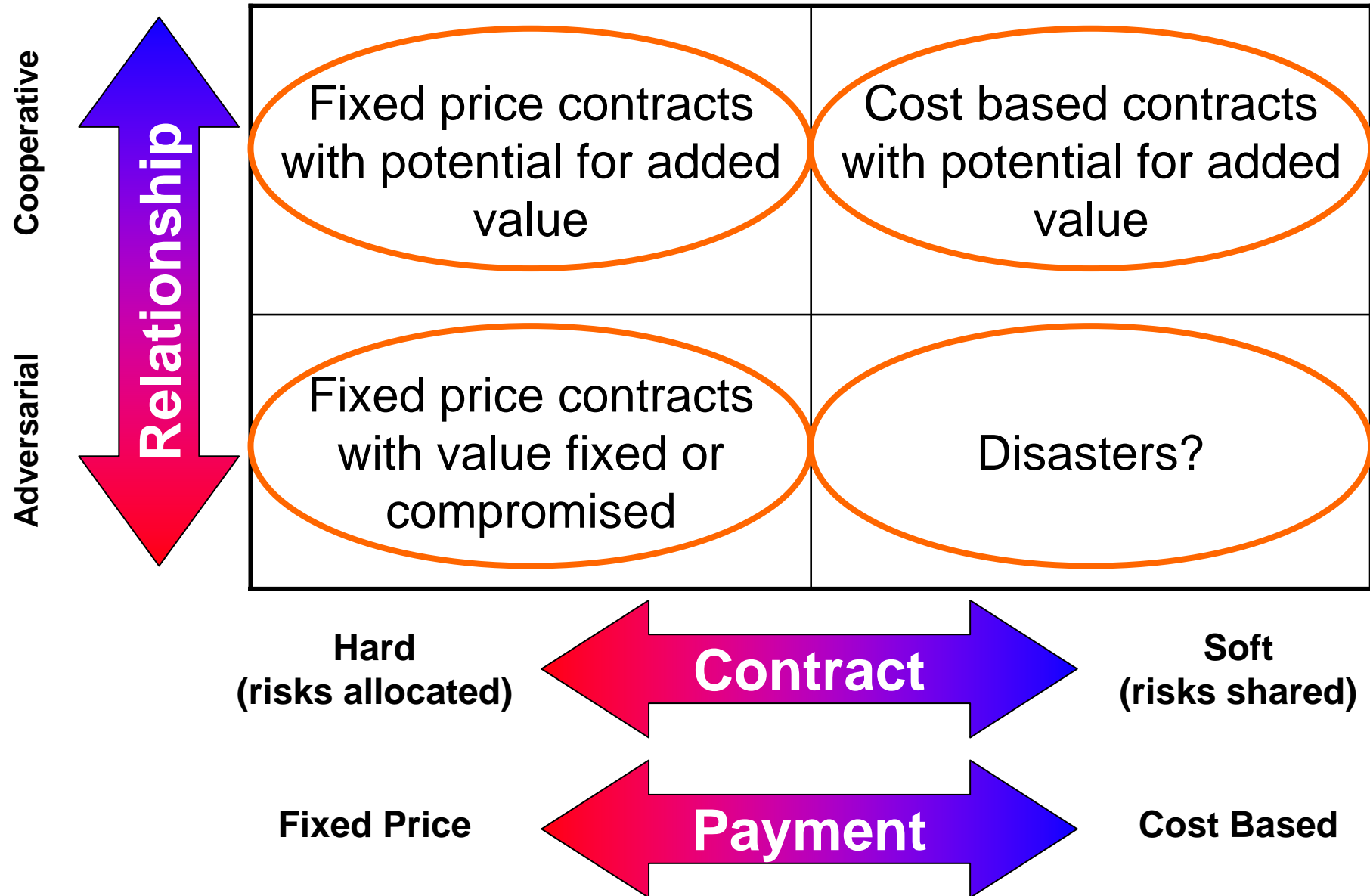
PPPs – Modifications / Variations



PPPs – Modifications / Variations

- + If the parties adopt an adversarial approach because this is a “hard money” contract:
 - How can they add value when they are at each other’s throats?
 - In most case they can’t, unless there’s a thaw in the relationship
- + If the parties instead adopt a cooperative approach:
 - How can they ensure they are not on the losing side of “win-lose” modifications and variations?
 - Through robust and effective contract management
- + This logic applies to all contracts, not just PPPs!

Contract Types – A New View



Contract Types – A New View

- + Some “hard” fixed-price contracts are now being managed using “soft” techniques
 - Example: VicRoads using an Alliance relationship management structure on a design & construct contract
- + Gateway Procurement Guidelines released last week provide a current approach for selecting an appropriate contract type
 - See: www.dtf.vic.gov.au
 - > Gateway Reviews and Best Practice Guidelines
 - > Lifecycle Guidance Material
 - > Procurement Guidelines

Contract Types – A New View

- + Contract models are now being identified on a project by project basis:
 - What will enable most efficient and effective management of the risks of the project?
 - Contract managers can seek to enhance value, regardless of the model
- + “THE State Government is... [deciding] how to build its proposed \$3.1 billion Wonthaggi [desalination] plant. Advice is being prepared for Cabinet that will weigh the relative merits of three options...”
 - Herald-Sun, 16 July 2007

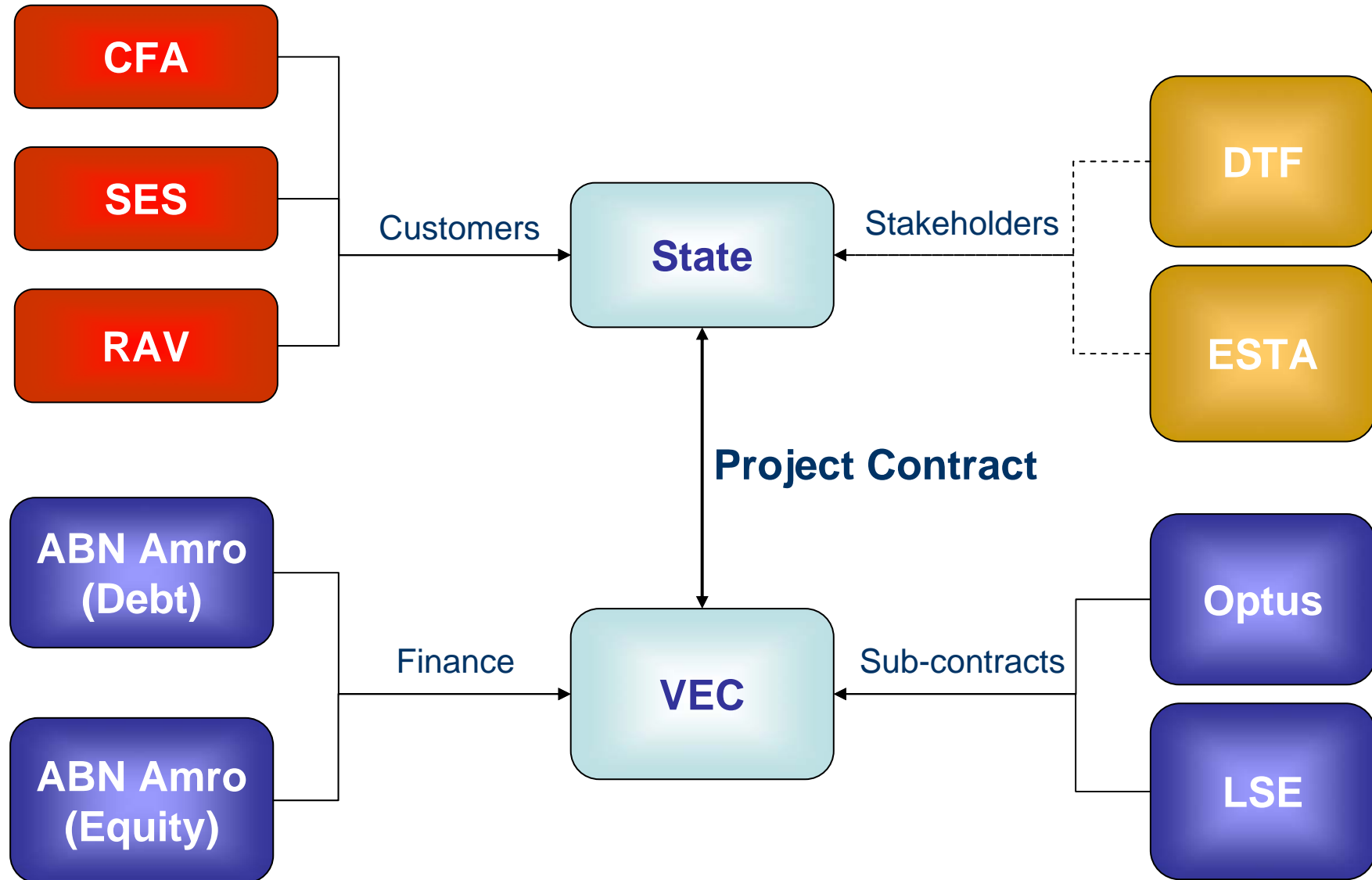
Contract Management – Some Issues

- + Enforcing the contract
- + Single points of contact
- + People/firms changing sides
- + Shopping lists

Maintaining value – Enforcing the contract

- + A well structured payment mechanism promotes the value outcome agreed in the contract
 - Provided it is enforced, where appropriate
 - KPI breaches can be waived, but ensure that an inappropriate precedent is not created
- + Where there are no payment reductions, the contractor will boast about this:
 - See the Case Studies at www.infrastructure.org.au
- + Where there are reductions, relationship management comes to the fore

Single points of contact – EAS Project



Single points of contact

- + Major contracts may have many interested parties on either side of the contract, each with their own agendas
- + Different pairs of interested parties will have different relationships (e.g. DTF with ABN Amro)
- + Formal contract communications should be channelled through a single point of contact
- + Where necessary, define what interaction can occur through informal channels (as done by government stakeholders in for the Melbourne Convention Centre project)

People/Firms Changing Sides – Probity Issues

- + For complex and unusual contracts, some segments of the subcontractor or adviser markets may be limited
- + Advisers may also move between firms
- + Example:
 - Melbourne office of Firm X provides commercial advice to government during tender process
 - Sydney office of Firm X subsequently advises the contractor in relation to financing issues

People/Firms Changing Sides – Probity Issues

- + Perceived conflicts can be managed in appropriate instances to enable parties to get the right advice or subcontractors, without compromising probity
- + See the Disclosure and Management of Conflicts of Interest Advisory Note at www.partnerships.vic.gov.au

Enhancing value – Shopping lists

- + Some modifications / variations may not be acceptable to the other party, or if implemented on their own, the costs of implementation may outweigh the benefits
- + By keeping a “shopping list” of these items, the contract manager can add value through seeking agreement for the implementation of the modification / variation upon:
 - It later becoming acceptable to the other party; or
 - Costs falling or benefits increasing.

Shopping list – Modification becomes acceptable

- + Wastewater treatment project had been operating successfully for several years, with occasional minor non-compliances in one area
- + Contractor unwilling to upgrade plant to prevent future non-compliances
- + Contractor's parent company subsequently seeks to sell the contractor – agrees to upgrade plant first to secure consent from government party and agreement from purchaser

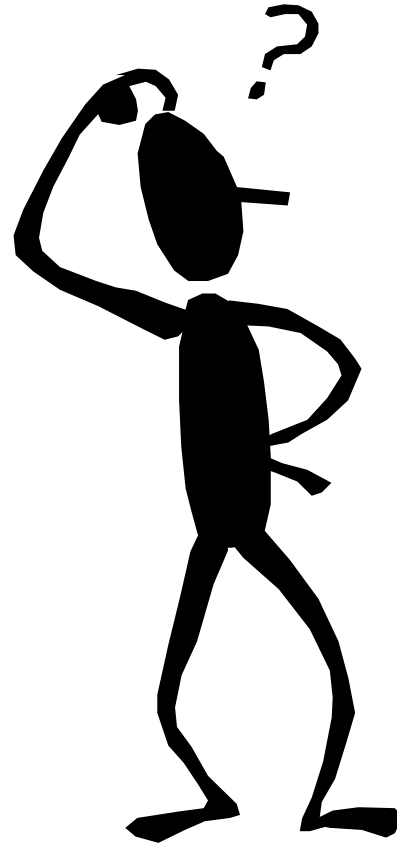
Shopping list – Costs decrease

- + Contractor provides equipment for emergency services vehicles
- + Government enquires about minor upgrade to the equipment (requires a contract variation)
 - Cost and inconvenience of accessing vehicles for this alone would outweigh benefit of upgrade
- + Contractor subsequently identifies a defect in the equipment and proposes to access all vehicles to repair this
 - Minor upgrade can be done at the same time
 - Cost may depend upon relationship quality

Summary

- + Whatever type of contract you are managing, the right relationship can create a value-adding environment
- + Areas to pay attention to include:
 - Enforcing the contract
 - Single points of contact
 - People/firms changing sides
 - Shopping lists

Questions?



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